

**FINANCIAL STATEMENTS
DECEMBER 31, 2006**

HARBOR BEACH COMMUNITY FIRE PROTECTION ASSOCIATION

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CPA's On Your Team

INDEPENDENT AUDITOR'S REPORT

Harbor Beach Community Fire
Protection Association
Harbor Beach, Michigan 48441

We have audited the accompanying financial statements of the business-type activities of the Harbor Beach Community Fire Protection Association, Harbor Beach, Michigan, as of and for the year ended December 31, 2006, which comprise the Association's basic financial statements as listed in the table of contents. These financial statements are the responsibility of Harbor Beach Community Fire Protection Association, Harbor Beach, Michigan's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the business-type activities of the Harbor Beach Community Fire Protection Association, Harbor Beach, Michigan, as of December 31, 2006, and the respective changes in financial position and cash flows, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis on pages 2 through 4 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Nietzke & Faupel, PC
NIETZKE & FAUPEL, P.C.
PIGEON, MICHIGAN

September 27, 2007

HARBOR BEACH COMMUNITY FIRE PROTECTION ASSOCIATION

MANAGEMENT'S DISCUSSION AND ANALYSIS FOR THE YEAR ENDED DECEMBER 31, 2006

Introduction

The discussion and analysis of Harbor Beach Community Fire Protection Association financial performance provides an overview of the Association's financial activities for the year ended December 31, 2006. This report is a part of the Association's Annual Report.

The purpose of the Association is to provide fire protection, emergency medical services, and other related services to the City of Harbor Beach and Sand Beach Township. The funding and operation of the Association remains the same under the agreement between the Association and each constituent unit. The Association is overseen by the Governing Board which consists of two trustees from each constituent unit and a member selected at large. The major source of funding for the Association is by an annual subsidy provided by each constituent unit. The formula consists of SEV of real and personal property, including industrial facilities tax, number of housing units, number of road miles, number of fire runs and population per constituent. These dollars are budgeted by the Association and then approved by the Association's Governing Board, the City council and the Township board.

Using the Annual Report

This annual report consists of a series of financial statements as follows:

- ▶ **The Statement of Net Assets** presents information on all of the Association's assets and liabilities, with the difference between the two reported as net assets.
- ▶ **The Statement of Revenue, Expenses and Changes in Net Assets** presents information showing how the Board's net assets changed during the most recent year. All changes in net assets are reported on an accrual basis, that is, the event is recorded in the accounting records when the underlying event takes place regardless of the timing of the related cash flows.
- ▶ **The Statement of Cash Flows** presents the financial activities of the Association on a cash received and cash paid basis. This statement also reconciles the change in cash accounts for the Board from the prior year to the current year.
- ▶ **Notes to the Financial Statements** provide additional details underlying the data provided in the financial statements.

Financial Highlights

The Statement of Net Assets outlines the assets, liabilities and net assets of the Association. The total assets increased from \$407,314 in the prior year to \$463,043 in the current year, an increase of \$55,729. The current year assets include:

	12/31/06		12/31/05	
Unrestricted current assets				
(cash, investments, and receivables)	\$ 103,644	22.38%	\$ 80,556	19.99%
Capital Assets	<u>359,399</u>	<u>77.62%</u>	<u>326,758</u>	<u>80.01%</u>
Total Assets	\$ <u>463,043</u>	<u>100.00%</u>	\$ <u>407,314</u>	<u>100.00%</u>

HARBOR BEACH COMMUNITY FIRE PROTECTION ASSOCIATION

MANAGEMENT'S DISCUSSION AND ANALYSIS FOR THE YEAR ENDED DECEMBER 31, 2006

The change in assets from the prior year were:

	12/31/06	12/31/05
Unrestricted current assets (cash, investments, and receivable)	\$ 23,088	\$ 19,194
Capital Assets	<u>32,641</u>	<u>26,713</u>
Total Change in Assets	\$ <u>55,729</u>	\$ <u>45,907</u>

The total liabilities increased from \$2,184 to \$49,103. This increase is due to the accounts payable and the note payable to Eastern Huron Ambulance for \$45,000 for the purchase of land.

The change in net assets of \$8,810 as shown on the Statement of Revenues, Expenses, and Changes in Net Assets includes:

	12/31/06	12/31/05
Operating income (loss)		
(operating revenues less operating expenses)	\$ 5,043	\$ (14,190)
Non-Operating Revenues	<u>3,767</u>	<u>58,165</u>
Change in Net Assets	\$ <u>8,810</u>	\$ <u>43,975</u>

This change in net assets increased the net assets from \$405,130 at the beginning of the year to \$413,940 at the end of the year. The total net assets includes \$314,399 for capital assets net of related debt, with the remainder amount \$99,541 unrestricted.

The Association realizes nearly all of its operating revenue is from the annual subsidy from the City of Harbor Beach and Sand Beach Township. The City of Harbor Beach in the amount of \$50,562 comprise 43% of the revenue while the subsidy from Sand Beach Township in the amount of \$49,786 comprise 43% and the remaining 14% is from miscellaneous income. Total operating revenue increased by \$17,552 or 18% from the prior year. The relative percentages for sources of revenue did not change significantly from one year to the next.

The largest expense is depreciation making up \$37,400 or 33.40% of the expenses. Insurance in the amount of \$16,525 represent 14.75% of the expenses. Personal services and materials makes up the remaining \$58,065 or 51.85% of the total expenses. Total operating expenses decreased \$1,681 or 1.5 % from the prior year due to the decrease in depreciation expense, repairs and maintenance and wages.

The non-operating revenue of the prior year was \$58,165 as compared to \$3,767 in the current year. The interest income portion of non-operating revenue was \$1,243 in the prior year compared to \$5,601 in the current year. There was a FEMA grant received during 2005 that accounts for most of difference between the years.

During the year 2006, there were no significant variations between the actual revenues and expenses and the budgeted revenues and expenses as approved by the Governing Board, the City Council, and the Township Board. The overall financial position of the Association has not significantly changed from the prior year as the agreement for services and funding between the Association, the City, and the Township has remained fundamentally the same.

HARBOR BEACH COMMUNITY FIRE PROTECTION ASSOCIATION

MANAGEMENT'S DISCUSSION AND ANALYSIS FOR THE YEAR ENDED DECEMBER 31, 2006

Requests for Information

This financial report is designed to provide citizens of the City of Harbor Beach and Sand Beach Township with a general overview of the Association's finances and to show accountability for the funding it receives. Questions concerning any of the information in this report should be addressed to:

Marilyn Townley, Secretary/Treasurer
Harbor Beach Community Fire Protection Association
Harbor Beach, MI 48441

BASIC FINANCIAL STATEMENTS

HARBOR BEACH COMMUNITY FIRE PROTECTION ASSOCIATION

STATEMENT OF NET ASSETS DECEMBER 31, 2006

Current assets:

Cash and investments	\$ 103,644
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Non-current assets:**Capital assets:**

Land (Non-depreciated)	78,544
Buildings	148,650
Equipment	787,592
Accumulated depreciation	(655,387)

Total non-current assets, net of accumulated depreciation	359,399
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Total assets

463,043

Current liabilities:

Accounts payable	3,963
Accrued payroll liabilities	140
Current portion of long-term debt	22,500
Total current liabilities	26,603

Long-term liabilities:

Note payable - Eastern Huron Ambulance	22,500
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Total liabilities

49,103

Net assets:

Investment in capital assets, net of related debt	314,399
Unrestricted	99,541
Total net assets	\$ 413,940

HARBOR BEACH COMMUNITY FIRE PROTECTION ASSOCIATION

**STATEMENT OF REVENUE, EXPENSES, AND CHANGE IN NET ASSETS
FOR THE YEAR ENDED DECEMBER 31, 2006**

OPERATING REVENUES:

Operating contributions:

City of Harbor Beach	\$ 50,562
Sand Beach Township	49,786
Miscellaneous income	16,685

Total operating revenue	<u>117,033</u>
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OPERATING EXPENSES:

Advertising and promotional	834
Capital outlay	2,239
Depreciation expense	37,400
Education and milage	1,010
Fuel	2,042
Insurance	16,525
Memberships and dues	215
Miscellaneous expense	1,179
Professional fees	2,460
Repairs and maintenance	7,766
Supplies	3,021
Taxes - FICA	2,363
Telephone	2,081
Utilities	7,202
Wages	25,654

Total operating expenses	<u>111,990</u>
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Operating income	<u>5,043</u>
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NON-OPERATING REVENUES (EXPENSES):

Interest income	5,601
(Loss) on disposal of assets	(1,834)

Total non-operating revenues	<u>3,767</u>
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CHANGE IN NET ASSETS	8,810
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NET ASSETS AT JANUARY 1, 2006	<u>405,130</u>
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NET ASSETS AT DECEMBER 31, 2006	<u><u>\$ 413,940</u></u>
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HARBOR BEACH COMMUNITY FIRE PROTECTION ASSOCIATION

STATEMENT OF CASH FLOWS FOR THE YEAR ENDED DECEMBER 31, 2006

CASH FLOWS FROM OPERATING ACTIVITIES:

Cash received from township and city for fire service	\$ 100,348
Cash received from miscellaneous income	16,685
Cash payments to employees	(25,654)
Cash payments to suppliers for materials and services	(47,016)
Net cash provided by operating activities	<u>44,363</u>

CASH FLOWS FROM CAPITAL AND RELATED

FINANCING ACTIVITIES:

Capital assets purchased	(26,875)
Land	(45,000)
Increase in long-term liabilities	22,500
Current portion of long-term debt	22,500
Net cash (used) by capital and related financing activities	<u>(26,875)</u>

CASH FLOW FROM INVESTING ACTIVITIES:

Interest income	<u>5,600</u>
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NET INCREASE IN CASH 23,088

CASH AT JANUARY 1 80,556

CASH AT DECEMBER 31 **\$ 103,644**

Reconciliation of operating income to net cash flows from operating activities:

Operating income	\$ 5,043
Add depreciation expense	37,400
Changes in current assets and current liabilities:	
Increase (decrease) in current liabilities:	
Accrued payroll	(358)
Accounts payable	2,278

Net cash provided by operating activities **\$ 44,363**

HARBOR BEACH COMMUNITY FIRE PROTECTION ASSOCIATION

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2006

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

The financial statements of the Association have been prepared in conformity with accounting principles generally accepted in the United States of America as applied to enterprise funds of governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles.

Reporting Entity

The Association was formed pursuant to the terms of an interlocal agreement dated September 10, 1984. The Association began operations February 1, 1985 and its purpose is to provide fire protection to the residents and property owners of the constituent units which include the City of Harbor Beach and Sand Beach Township in Huron County, Michigan.

The Association operates under an appointed Board. The Board consists of two representatives from each constituent unit. All representatives are appointed by their respective governing bodies by resolution and serve following appointment until a successor is appointed. Any constituent unit may appoint an alternate member who may sit on the Board in the absence of a regular member and have all of the powers and duties of a regular member. A Board member is eligible for re-appointment at the expiration of his or her term of office. A Board member must be a resident of the constituent unit which he or she represents. A Board member shall not be an employee of any fire department of the Association. Each year the Board selects one additional Board member who must also be a resident of one of the constituent units.

In accordance with generally accepted accounting principles and Governmental Accounting Standards Board (GASB) Statement No. 14 "The Financial Reporting Entity", these financial statements present the funds of the Board. The criteria established by the GASB for determining the reporting entity includes oversight responsibility, fiscal dependency, and whether the financial statements would be misleading, if data were not included. Based on the criteria, there are no component units which should be included in the financial statements of the Harbor Beach Community Fire Protection Association.

Measurement Focus, Basis of Accounting and Basis of Presentation

The Association is presented as an enterprise fund. The financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recognized when the liability is incurred or an economic asset is used. Revenues, expenses, gains, losses, assets and liabilities resulting from exchange and exchange-like transactions are recognized when the exchange takes place.

The Association follows all pronouncements of the Governmental Accounting Standards Board, and has elected not to follow Financial Accounting Standards Board pronouncements issued after November 30, 1989.

HARBOR BEACH COMMUNITY FIRE PROTECTION ASSOCIATION

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2006

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES: (CONTINUED)

Measurement Focus, Basis of Accounting and Basis of Presentation: (Continued)

Preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Cash and Cash Equivalents

For purposes of the statement of cash flows, cash and cash equivalents have original maturities of three months or less from the date of acquisition.

Capital Assets

Capital assets of the Board are reported at cost or the fair market value at the time of contribution to the Association. Capital assets in service are depreciated using the straight-line method over the following useful lives:

	Years
Buildings	10-40
Equipment	5-20

NOTE 2 - DEPOSITS AND INVESTMENTS:

Deposits are carried at cost. Deposits of the Association are made in banks in the name of the Harbor Beach Fire Department. Michigan Compiled Laws, Section 129.91, as amended by Public Act 196 of 1997, authorizes the Board Treasurer to deposit and invest in the accounts of federally insured banks, credit unions, and savings and loan associations; bonds, securities, and direct obligations of the United States, or any agency or instrumentality of the United States in which the principal and interest is fully guaranteed by the United States, including securities issued or guaranteed by the Government National Mortgage Association; United States government or Federal agency obligation repurchase agreements; bankers' acceptance of United States banks; mutual funds composed of investment vehicles which are legal for direct investment by local units of government in Michigan; and commercial paper rated by two standard rating agencies within the two highest classifications, which matures not more than 270 days after the date of purchase. The Association's deposits are in accordance with statutory authority. The Association does not have a deposit or investment policy.

HARBOR BEACH COMMUNITY FIRE PROTECTION ASSOCIATION

NOTES TO FINANCIAL STATEMENTS DECEMBER 31, 2006

NOTE 4 – LONG-TERM LIABILITY:

The long-term liability consists of a non-interest bearing note payable to Eastern Huron Ambulance dated October 11, 2006, for the purchase of land with a balance of \$45,000 at December 31, 2006. This note matures on September 30, 2008 and is due in two annual payments of \$22,500. If the any portion of the note is not repaid by September 30, 2008, interest at a fixed rate of 6% will begin to accrue on the sum of the unpaid portion.

Payment schedule follows:

<u>Year</u>	<u>Amount Due</u>
2007	\$ 22,500
2008	22,500
Total	<u>\$ 45,000</u>

NOTE 5 – SUBSIDY REVENUE:

In the event that it is necessary to finance all or any part of the operation fund or capital expenditures of the Association by contribution, the contribution to be made to the Association each constituent unit shall be equal to that percentage or proportion which each constituent bears to the whole of the Association based upon the following formula: state equalized value of real and personal property, including industrial facilities tax (70%); population (10%); number of dwelling units (10%); number of fire runs (5%); and miles of roads (5%). State equalized values and dwelling units shall be based upon the most recently completed U.S. Bureau of the Census Report. The number of fire runs shall be based upon the most recently completed prior five-year period. To be binding upon a constituent unit, any contribution must be authorized by resolution of the governing body of that constituent unit. The failure of the governing body of any constituent unit to authorize its contribution to the Association and/or to pay the same in full to the Association within thirty days of the commencement of the Association's fiscal year shall operate as an immediate withdrawal of that constituent unit from the Association.

Contributions for the year ended December 31, 2006 were \$50,562 and \$49,786 for the City of Harbor Beach and the Township of Sand Beach, respectively.

NOTE 6 - RISK MANAGEMENT:

The Association is exposed to various risks of loss related to property loss, torts, errors and omissions, employee injuries, and natural disasters. The Association is insured with Volunteer Fireman's Insurance Services, Inc. for claims related to property loss, general liability, errors and omissions and auto liability. The Association also participates in the Michigan Municipal Worker's Compensation Fund for claims related to workers compensation.



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Principals: Eugene R. Gascho, COO
Brian V. Hazard, CPA JoAnn E. Lakie, CPA

Members of: Michigan Association of Certified Public Accountants • American Institute of Certified Public Accountants
September 27, 2007

CPA's On Your Team

To the Members of the Association
Harbor Beach Community Fire
Protection Association
Harbor Beach, Michigan

The following comments relate to situations brought to our attention during the course of our recent audit of the financial statements of the Harbor Beach Community Fire Protection Association for the year ended December 31, 2006 and are submitted for your evaluation and consideration. We would like to emphasize that our audit was conducted for the purpose of expressing opinions on the aforementioned financial statements; therefore, the following comments are not necessarily all-inclusive.

Off-site Back-up of Records:

Currently, the Association's records are backed up and kept at the same location as the original records. We would recommend developing a disaster recovery plan and keeping a back-up of all the Association's records at an off-site location.

Capitalization Policy:

During our audit, we noted that the Association has no formal policy for the capitalization of property and equipment purchases. This leaves the possibility that a capital asset will not be appropriately recorded. We suggest that the Association implement a written policy requiring all assets costing more than an established amount, such as \$1,000, to be capitalized and depreciated over the assets useful life.

Investment policy under GASB 40:

During the course of our audit, it was noted that the Association has not amended their investment policy to address the various areas of risk as described by GASB Statement No. 40. Deposit and investment resources often represent significant assets of the Association's funds. These resources are necessary for the delivery of the Association's services programs. GASB Statement No. 40 is designed to inform financial statement users about deposit and investment risks that could affect the Association's ability to provide services and meet its obligations as they become due.

We recommend the Board review their current investment policy and make the necessary amendments to address custodial credit risk, concentration of credit risk, interest rate risk, and foreign currency risk, if applicable. Such policies are required to be disclosed in the notes to the Association's financial statements by GASB Statement No. 40.

The above recommendations are being made in an effort to improve the Association's system of record keeping. If you have any questions regarding these recommendations, please contact us.

Nietzke & Faupel, PC
Nietzke & Faupel, PC
Pigeon, Michigan

Communication of Significant Deficiencies and Material Weaknesses

September 27, 2007

To the Members of the Association
of the Harbor Beach Community Fire Protection Association,

In planning and performing our audit of the financial statements of the business-type activities of Harbor Beach Community Fire Protection Association as of and for the year ended December 31, 2006, in accordance with auditing standards generally accepted in the United States of America, we considered Harbor Beach Community Fire Protection Association's internal control over financial reporting (internal control) as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the governmental unit's internal control. Accordingly, we do not express an opinion on the effectiveness of the governmental unit's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control that we consider to be significant deficiencies and other deficiencies that we consider to be material weaknesses.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or a combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the following deficiencies to be significant deficiencies in internal control:

Due to the limited number of people sitting on the Association's board, many critical duties are combined and given to the available members. Presently, a single individual prepares and signs checks, reconciles bank accounts, as well as maintains the general ledger. Also, the same person responsible for cash disbursements is responsible for handling and depositing of cash receipts and posts to the cash receipts and maintains the accounts receivable subsidiary. Members who have both custodial and record keeping responsibilities for the same asset create a significant internal control deficiency.

While we understand that a complete segregation of duties is impractical for a small board with limited personnel, we believe that some relatively minor changes could be made which would significantly improve controls. To the extent possible, duties should be segregated to serve as a check and balance on the member's integrity and to maintain the best control system as possible. We suggest that the duties of cash disbursements and cash receipts are separated from the duties of the bank account reconciliation.

Our audit process disclosed that the Signature Bank checking account was not updated in a timely manner to reflect changes in authorized check signers. A former board chairman was still listed on the signature card. This is a major oversight and increases the potential for abuse. Only current authorized association officers should be responsible for such an important control over cash disbursements. In an effort to maintain stronger internal controls, we suggest that management annually review and approve the authorized check signers on record with the bank and make any necessary updates as soon as possible.

A material weakness is a significant deficiency, or a combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

The AICPA Auditing Standards Board issued Statements on Audit Standards (SAS) 112 which establishes standards and provides guidance on communicating matters related to an entity's internal control over financial reporting and is effective for periods ending after December 15, 2006. According to SAS 112, it is considered to be a control deficiency if a client we are auditing has ineffective controls over the preparation of their financial statements such that client controls are absent or controls are not effective in preventing or detecting material misstatements in the preparation of the financial statements, including the related footnotes.

The personnel of Harbor Beach Community Fire Protection Association have the capability to perform monthly internal accounting functions and reports as required by management. The personnel of Harbor Beach Community Fire Protection Association do not have the expertise to prepare the annual financial statements and related footnotes in accordance with the method of accounting utilized in the external audit report. We believe this meets the definition of a material weakness under Statement on Auditing Standards 112.

This communication is intended solely for the information and use of management, the Board of Operations of Harbor Beach Community Fire Protection Association, and others within the organization, and is not intended to be and should not be used by anyone other than these specified parties.

Nitzke & Fausel, PC

Nietzke & Faupel, PC
Pigeon, Michigan

September 27, 2007